84-2006

No. ——

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1984

DON C. JOHNSON and ELIZABETH A. JOHNSON,
Petitioners,

v.

MILTON RIGHETTI, GLORIA RIGHETTI,
MILTON E. RIGHETTI, MICHAEL RIGHETTI,
MARILYN RIGHETTI, and MARY ANN RIGHETTI,
Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

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June 26, 1985

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QUESTIONS PRESENTED FOR REVIEW

1. Whether the "enforceable contract" exception to the "American Rule" on attorney's fees is only applicable in diversity cases.

2. Whether the federal bankruptcy statute on relief from the automatic stay against foreclosure preempts the state statutory scheme and the debtor and creditor's contract to deprive the bankruptcy judge of the discretion to award attorney's fees to the successful party.

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Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

The Petitioners, Don C. Johnson and Elizabeth A. Johnson respectfully pray that a Writ of Certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Ninth Circuit entered on March 28, 1985.

OPINION BELOW

The opinion of the Court of Appeals is reported as *Johnson v. Righetti*, 756 F.2d 738 (9th Cir. 1985). A copy appears in the appendix.

JURISDICTION

The judgment of the United States Court of Appeals for the Ninth Circuit was entered on March 28, 1985 and this petition was filed within 90 days of that date.

The court's jurisdiction is invoked under 28 U.S.C. § 1254(1).

STATUTORY PROVISIONS INVOLVED

United States Code, Title 11:

Section 362. *Automatic Stay*

a) Except as provided in subsection (b) of this section, a petition filed under section 301, 302, or 303 of this title, or an application filed under section 5(a)(3) of the Securities Investor Protection Act of 1970 (15 U.S.C. 78eee(a)(3)), operates as a stay, applicable to all entities, of—

(1) The commencement or continuation, including the issuance or employment of process, of a judicial, administrative, or other action or proceeding against the debtor that was or could have been commenced before the commencement of the case under this title, or to recover a claim against the debtor that arose before the commencement of the case under this title;

(2) the enforcement, against the debtor or against property of the estate, of a judgment obtained before the commencement of the case under this title;

(3) any act to obtain possession of property of the estate or of property from the estate or to exercise control over property of the estate;

(4) any act to create, perfect, or enforce any lien against property of the estate;

(5) any act to create, perfect, or enforce against property of the debtor any lien to the extent that such lien secures a claim that arose before the commencement of the case under this title;

(6) any act to collect, assess, or recover a claim against the debtor that arose before the commencement of the case under this title;

(7) the setoff of any debt owing to the debtor that arose before the commencement of the case under this title against any claim against the debtor; and

(8) the commencement or continuation of a proceeding before the United States Tax Court concerning the debtor.

* * * *

(d) On request of a party in interest and after notice and a hearing, the court shall grant relief from the stay provided under subsection (a) of this section, such as by terminating, annulling, modifying, or conditioning such stay—

(1) for cause, including the lack of adequate protection of an interest in property of such party in interest; or

(2) with respect to a stay of an act against property under subsection (a) of this section, if—

(A) the debtor does not have an equity in such property; and

(B) such property is not necessary to an effective reorganization.

Section 506. *Determination of Secured Status*

(b) To the extent that an allowed secured claim is secured by property the value of which, after any recovery under subsection (c) of this section, is greater than the amount of such claim, there shall be allowed to the holder of such claim, interest on such claim, and any reasonable fees, costs, or charges provided for under the agreement under which such claim arose.

California Civil Code:

Section 1717. *Contract Provision for attorney's fees; Award*

(a) In any action on a contract, where the contract specifically provides that attorney's fees and costs, which are incurred to enforce the provisions of that contract, shall be awarded either to one of

the parties or to the prevailing party, then the party who is determined to be the prevailing party, whether he or she is the party specified in the contract or not, shall be entitled to reasonable attorney's fees in addition to costs and necessary disbursements.

Where a contract provides for attorney's fees, as set forth above, such provision shall be construed as applying to the entire contract, unless each party was represented by counsel in the negotiation and execution of the contract, and the fact of the representation is specified in the contract.

Reasonable attorney's fees shall be fixed by the court, upon notice and motion by a party, and shall be an element of the costs of suit.

Attorney's fees provided for by this section shall not be subject to waiver by the parties to any contract which is entered into after the effective date of this section. Any provision in any contract which provides for a waiver of attorney's fees is void.

(b) (1) The court, upon notice and motion by a party, shall determine who is the prevailing party, whether or not the suit proceeds to final judgment, except as provided in paragraph (2), the prevailing party shall be the party who is entitled to recover costs of suit.

(2) Where an action has been voluntarily dismissed or dismissed pursuant to a settlement of the case, there shall be no prevailing party for purposes of this section.

Where the defendant alleges in his or her answer that he or she tendered to the plaintiff the full amount to which he or she was entitled, and thereupon deposits in court, for the plaintiff, the amount so tendered, and the allegation is found to be true, then the defendant is deemed to be a prevailing party within the meaning of this section. [Amended Stats 1983 ch 1073 § 1.]

California Civil Code Section 1717 was amended in 1983, effective January 1, 1984, by adding the second paragraph of subdivision (a).

STATEMENT OF THE CASE

Petitioners Don. C. Johnson and Elizabeth A. Johnson ("the Johnsons") filed a petition for reorganization under Title 11 of the United States Code, in the United States District Court of the Northern District of California. Respondents Milton Righetti, Gloria Righetti, Milton E. Righetti, Michael Righetti, Marilyn Righetti and Mary Ann Righetti ("the Righettis") were secured creditors. The Righettis held a promissory note secured by a first deed of trust on a 76 acre parcel of real property.

The Righettis filed a complaint for relief from the automatic stay seeking to foreclose under their deed of trust.

The bankruptcy court had jurisdiction over the complaint for relief from stay pursuant to Section (c)(1) of the Emergency Interim Bankruptcy Rule adopted by the United States District Court for the Northern District of California, effective December 25, 1985 (the "Emergency Rule"), and 11 U.S.C. Section 362(d).

The bankruptcy court found the complaint for relief from stay was frivolous:

> The Court: Well, the thing is that there is overwhelming protection, not just adequate protection, there is overwhelming protection in relation to that. The first deed of trust balance of forty-eight, forty-nine, fifty thousand, whatever it is, is so well protected that it's silly for us even to waste time. The relief is denied.

Transcript of Relief from Stay Trial, August 18, 1984, p. 6, Item No. 1, Clerk's Record on Appeal to Ninth Circuit.

The bankruptcy court awarded reasonable attorneys fees to the Johnsons under the attorney fee provisions in the promissory note and deed of trust. (See appendix, Findings of Fact, Conclusions of Law and Order for Judgment, filed August 30, 1983 and Order Denying Relief From Automatic Stay, entered September 2, 1983.

The attorney's fee provisions in the note and deed of trust were unilateral provisions which by law are mutually enforceable in California. Calif. Civil Code Section 1717. (Copies are reproduced in the appendix.)

The Righettis appealed the judgment to the United States District Court for the Northern District of California. The United States District Court, Northern District, had jurisdiction over the appeal from bankruptcy court under Section (3) of the Emergency Rule. The district court affirmed the judgment denying relief from the automatic stay but reversed the award of attorneys' fees. (See appendix, Order Affirming In Part And Reversing In Part The Decision Of The Bankruptcy Court, filed February 16, 1984.) The district court held that an action under 11 U.S.C. 362(d) was an action on a statute, not on contract, and denied recovery of fees under the contractual provision, holding that Civil Code Section 1717 was not applicable. The Johnsons filed a timely petition for rehearing which the district court denied, maintaining that an action under 11 U.S.C. § 362(d) is not an action on a contract, although acknowledging it is certainly a prerequisite to any action by the creditor on the contract.

The Johnsons filed a timely appeal to the United States District Court for the Ninth Circuit, which affirmed the district court's ruling, holding that only in diversity cases does the "American Rule" permit an award of attorney's fees based on the contract between the parties.

REASONS FOR GRANTING THE WRIT

I. THE NINTH CIRCUIT'S DECISION TO REVERSE THE BANKRUPTCY COURT'S AWARD OF ATTORNEY'S FEES UNDER THE CONTRACTS BETWEEN THE PARTIES IS IN CONFLICT WITH THE DECISIONS OF THIS COURT INTERPRETING THE "AMERICAN RULE" ON ATTORNEY'S FEES.

The contracts between the parties in this case were enforceable contracts which provided for recovery of attorney's fees by the prevailing party in litigation affecting the contracts. Calif. Civil Code § 1717.

This court has long held that under the "American Rule" attorneys fees are generally not recoverable absent statute or *enforceable contract. Alyeska Pipeline Serv. v. Wilderness Soc.*, 421 U.S. 240, 257, 44 L. Ed. 2d 141, 153, 95, S. Ct. 1612 (1975) ; *F.D. Rich Co. v. Industrial Lumber Co.*, 417 U.S. 116, 126, 40 L. Ed. 2d 703, 713, 94 S. Ct. 2157 (1974) ; *Hall v. Cole*, 412 U.S. 1, 4, 36 L. Ed. 2d 702, 707; 93 S. Ct. 1943; *Arcambel v. Wiseman*, 3 Dall 306, 1 L. Ed 613 (1796).

The Ninth Circuit refused to affirm the award of attorney's fees in this case even though the underlying contracts contained enforceable provisions for recovery of attorney's fees. Citing *Alyeska Pipeline*, supra, the Ninth Circuit interpreted the "American Rule" to restrict enforceability of attorney's fee provisions to diversity cases. *Johnson v. Righetti*, 756 F.2d 738, 741. The Ninth Circuit relied on footnote 31 of the *Alyeska Pipeline* decision which states:

> A very different situation is presented when a federal court sits in a diversity case. "[I]n an ordinary diversity case where the state law does not run counter to a valid federal statute or rule of court, and usually it will not, state law denying the right to attorney's fees or giving a right thereto, which re-

> flects a substantial policy of the state, should be followed . . .

Alyeska Pipeline, supra, 421 U.S. 259, n.31.

The Ninth Circuit failed to note this Court's discussion of the "American Rule" in the main body of the opinion:

> [T]he rule 'has long been that attorney's fees are not recoverable. . . .' Fleischmann Distilling Corp. 386 U.S., at 717, 18 L. Ed. 2d 475, 87 S. Ct. 1404. Other recent cases have also reaffirmed *the general rule that, absent statute or enforceable contract*, litigants pay their own attorneys' fees. . . . (emphasis added).

Alyeska Pipeline Serv., supra, 421 U.S. 257.

By ignoring the established exception to the American Rule, the Ninth Circuit improperly refused to affirm the award of attorney's fees to the Johnsons under the enforceable attorney's fee provisions in the note and deed of trust.

The decision of the Ninth Circuit is also open to serious question because it arbitrarily preempts California law on the interpretation of attorney's fee provisions in contracts of adhesion and it undermines the protection of the automatic stay of 11 U.S.C. § 362(a). (See sections 3 and 4 below.)

II. THE NINTH CIRCUIT INTERPRETED CALIFORNIA CIVIL CODE SECTION 1717 IN A MANNER WHICH CONFLICTS WITH THE HOLDINGS OF THE CALIFORNIA SUPREME COURT AND APPELLATE COURTS.

Interpretation of contractual attorney's fee provisions is a matter of state law. *Security Mortgage Co. v. Powers*, 278 U.S. 149, 153, 73 L. Ed 236, 49 S. Ct. 84 (1928); *In re Triangle Equipment Co., Inc.*, 26 B.R. 175, 177 (W.D. Va. 1982).

Under California law, the attorney's fees provisions in the contracts between the Johnsons and the Righettis gave the Johnsons the right to recover attorney's fees as the prevailing parties in the relief from stay action.

The Ninth Circuit based its interpretation of Section 1717 exclusively on the opening phrase of the statute, which says that it applies to "actions on a contract." The Ninth Circuit interpreted this phrase to mean attorneys fees are not recoverable in relief from stay litigation because it is an "action on a statute."

However, California courts have interpreted Section 1717 to provide *mutuality* of remedies. Under California case law, any party to an action who would be liable for attorney's fees pursuant to a provision in the contract if he loses, is entitled to recover attorneys fees if he wins. *Christensen v. Dewor Development*, 33 Cal. 3d 778, 191 Cal. Rptr. 8 (1983); *Reynolds Metals Co. v. Alperson*, 25 Cal. 3d 124, 158 Cal. Rptr. 1 (1979); *Jones v. Drain*, 149 Cal. App. 3d 484, 196 Cal. Rptr. 827, *Smith v. Krueger*, 150 Cal. App. 3d 752, 198 Cal. Rptr. 174; *MacKinder v. OSCA Development Co.*, 151 Cal. App. 3d 728, 198 Cal. Rptr. 864 (1984); *Nasser v. Superior Court*, 156 Cal. App. 3d 52, 202 Cal. Rptr. 552 (1984); *Lewis v. Alpha Beta*, 141 Cal. App. 3d 29, 189 Cal. Rptr. 840; *Berge v. International Harvester Co.*, 142 Cal. App. 3d 152, 190 Cal. Rptr. 815 (1983); *Saucedo v. Mercury Sav. & Loan Assn.*, 111 Cal. 3d 309, 168 Cal. Rptr. 552 (1980); *Care Construction Inc. v. Century Convalescent Centers, Inc.*, 54 Cal. App. 3d 701, 126 Cal. Rptr. 761 (1976).

Under Civil Code Section 1717, the Johnsons would have been entitled to recover attorneys fees as the prevailing party in the relief from stay action *because* the Righettis would have been entitled to recover their attorneys fees if they had prevailed.

The Righettis would have been able to recover their attorneys fees at the foreclosure sale as part of their secured debt, pursuant to the provisions of the deed of

trust, if they had been granted relief from the automatic stay. If they had obtained some relief short of foreclosure, they would have been entitled to recover their attorney's fees under 11 United States Code Section 506(b).

The bankruptcy courts have consistently held that attorneys' fees incurred in an action to obtain relief from the automatic stay are within the coverage of the standard deed of trust type provisions for recovery of attorneys' fees. *Matter of Calzaretta*, 35 B.R. 92 (Bkcy, N.D. Ill., E.D. 1983); *In re Marino*, 7 C.B.C. 182 (Bkcy. W.D. Mich. 1982); *In re Carey*, 8 B.R. 1001 (Bkcy. S.D. Ca. 1981).

Under the circumstances, Civil Code Section 1717 provides a basis for recovery of attorneys fees by the Johnsons as the prevailing party on the action for relief from the automatic stay.

III. THE DECISION BELOW UNNECESSARILY INTERPRETS FEDERAL BANKRUPTCY LAW TO PREEMPT STATE CONTRACT LAW. CIVIL CODE § 1717 MAKING ADHESIVE ATTORNEY FEE PROVISIONS MUTUALLY ENFORCEABLE AS A MATTER OF LAW IS BASED ON IMPORTANT PUBLIC POLICY CONSIDERATIONS. THE DECISION BELOW CALLS FOR AN EXERCISE OF THE COURT'S POWER OF SUPERVISION.

California Civil Code Section 1717 was enacted to prohibit the practice of including one-sided attorney's fees in contracts of adhesion. The statute is based on important public policy considerations:

> Civil Code Section 1717 is part of an overall legislative policy designed to enable consumers and others who may be in a disadvantageous contractual position to protect their rights through the judicial process by permitting recovery of attorney's fees incurred in litigation in the event they prevail.
>
> It is common knowledge that parties with superior bargaining power, especially in 'adhesion' type con-

> tracts, customarily include attorney fee clauses for their own benefit. This places the other contracting party at a distinct disadvantage. Should he lose in litigation, he must pay legal expenses of both sides and even if he wins, he must bear his own attorney's fees. One-sided attorney's fees clauses can thus be used as instruments of oppression to force settlements of dubious or unmeritorious claims.

Coast Bank v. Holmes, 19 Cal. App. 3d 581, 597, 97 Cal. Rptr. 30, footnote 3.

The Ninth Circuit's decision calls for an exercise of the Court's power of supervision because it unnecessarily preempts Civil Code Section 1717, although the statute reflects an important policy of the State of California and it does not run counter to any valid federal statute or rule of court.

IV. THE DECISION BELOW RAISES SIGNIFICANT AND RECURRING PROBLEMS IN THE ORDERLY ADMINISTRATION OF BANKRUPTCY CASES AND UNDERMINES THE IMPORTANT POLICIES BEHIND THE AUTOMATIC STAY.

The decision of the Ninth Circuit in this case undermines the fundamental policy considerations underlying the automatic stay of 11 U.S.C. Section 362.

> The automatic stay is one of the fundamental debtor protections provided by the bankruptcy laws. It gives the debtor a breathing spell from his creditors. It stops all collection efforts, all harassment, and all foreclosure actions. It permits the debtor to attempt a repayment or reorganization plan or simply to be relieved of the financial pressures that drove him into bankruptcy.
>
> The automatic stay also provides creditor protection. Without it, certain creditors would be able to pursue their own remedies against the debtor's property.
>
> Those who acted first would obtain payment of the claims in preference to and to the detriment of

> other creditors. Bankruptcy is designed to provide an orderly liquidation procedure under which all creditors are treated equally. A race of diligence by creditors for the debtors assets prevents that.

(H. Rept. No. 95-595, pp. 121, 340, Bkr.-L. Ed., Legislative History Sections 82:4, 82:16).

The Ninth Circuit's decision places creditors in a position to use attorney's fees as a means of coercing settlements in relief from stay cases by making unilateral an attorney's fee provision in the contract which would otherwise be mutually enforceable by its terms or, as in California, by law. The decision directly undermines the policy behind the automatic stay to stop all collection efforts, all harassment, and all foreclosure actions. It aids creditors to overcome the automatic stay so they can pursue their own remedies against the debtor's property, free of the control of the bankruptcy court.

Another adverse effect of the ruling is to thrust the burden of the attorneys fees for unsuccessful relief from stay litigation onto the unsecured creditors of the estate. Attorney's fees are administrative expenses and directly reduce the funds available to pay unsecured creditors.

CONCLUSION

For these reasons, a writ of certiorari should issue to review the judgment and opinion of the Ninth Circuit.

Respectfully submitted,

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June 26, 1985

APPENDIX

APPENDIX

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

Nos. 84-1811, 84-1817

D.C. Nos. C 83-5720 AJZ, C 84-0248 AJZ

IN RE: DON C. JOHNSON AND ELIZABETH A. JOHNSON,
Debtors.

DON C. JOHNSON AND ELIZABETH A. JOHNSON,
Appellants.

v.

MILTON RIGHETTI, GLORIA RIGHETTI,
MILTON E. RIGHETTI, MICHAEL RIGHETTI,
MARILYN RIGHETTI AND MARY ANN RIGHETTI,
Appellees.

Argued and Submitted February 14, 1985

Filed March 28, 1985

Appeal from the United States District Court
for the Northern District of California
Alfonso J. Zirpoli, District Judge, Presiding

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Bennett, Righetti & Johnson and Matthew Righetti, Oakland, California, for the appellees.

OPINION

Before: PREGERSON and FERGUSON, Circuit Judges, and GILLIAM,* District Judge.

FERGUSON, Circuit Judge:

The debtors, Dr. and Mrs. Johnson, appeal from the district court's reversal of the bankruptcy court's order awarding them attorney's fes incurred in opposing the creditors' unsuccessful motion for relief from the automatic stay. Because the bankruptcy court awarded attorney's fees in a relief from stay action, the disposition of which was governed entirely by federal law, pursuant to a state law which applied only to actions "on a contract," we affirm the district court's reversal of this award.

I

The Johnsons purchased from the Righetti family a parcel of land which comprises a cattle ranch. The Righettis hold a promissory note secured by a first deed of trust against this parcel.

In November 1982, after ceasing to make payments to the Righettis under the promissory note, the Johnsons filed a petition for reorganization under Chapter 11 of the United States Bankruptcy Code. In May 1983, the Johnsons still had not made any payments to the Righettis and the Righettis filed a request for relief from the automatic stay, pursuant to 11 U.S.C. § 362(d)(1), to foreclose upon their deed of trust. The Johnsons began payments again in July 1983. The bankruptcy court denied the Righettis' request for relief from the automatic stay and awarded attorney's fees to the Johnsons as the prevailing party under California Civil Code section 1717.

The Righettis appealed the bankruptcy court's decision to the district court. The district court affirmed the de-

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* The Honorable Earl B. Gilliam, United States District Judge for the Southern District of California, sitting by designation.

nial of the request or relief from the automatic stay but reversed the award of attorney's fees to the Johnsons. The Johnsons appeal the district court's order denying them attorney's fees.[1]

II

The bankruptcy court awarded the Johnsons attorney's fees incurred in opposing the Righettis' motion for relief from the automatic stay. It based this award upon California Civil Code section 1717. Section 1717 provides:

> *In any action on a contract,* where the contract specifically provides that attorney's fees and costs, which are incurred to enforce the provisions of that contract, shall be awarded either to one of the parties or to the prevailing party, then the party who is determined to be the prevailing party, whether he or she is the party specified in the contract or not, shall be entitled to reasonable attorney's fees in addition to costs and necessary disbursements.

Cal. Civ. Code § 1717(a) (emphasis added). Because the promissory note and deed of trust securing it provided that the Johnsons would pay any attorney's fees or costs the Righettis incurred in enforcing them, the bankruptcy court found section 1717 applicable and awarded attorney's fees to the party prevailing in the motion for relief from the automatic stay—i.e., the Johnsons.

The district court reversed the award of attorney's fees, finding that the bankruptcy court had ignored the opening phrase of section 1717 in awarding such fees in stay proceedings. On its face, section 1717 applies only to ac-

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[1] Because the order confirming the plan and discharging the debtors has been issued by the bankruptcy court, all proceedings in bankruptcy court are over. Therefore, because the final order has already occurred, *In re Mason*, 709 F.2d 1133, 1316 (9th Cir. 1983), we need not determine here whether an award of attorney's fees in an action for relief from the automatic stay is a final order appealable to this court. 28 U.S.C. § 1293(b).

tions "on a contract." The district court held that a request for relief from the automatic stay, brought under 11 U.S.C. § 362(d), is an action based on a federal statute and not on a contract.

The question for determination here, then, is whether a motion for relief from an automatic stay pursuant to 11 U.S.C. § 362(d) is an "action on a contract" to which California law should be applied. Although the Righettis were seeking relief from the automatic stay in order to foreclose under the deed of trust, both case law and the nature of stay relief proceedings support the conclusion that stay relief proceedings are not actions "on a contract" to which California law should be applied. *See In re Coast Trading Co.*, 744 F.2d 686, 693 (9th Cir. 1984) ("the question of the applicability of the bankruptcy laws to particular contracts is not a question of the enforceability of a contract but rather involves a unique, separate area of federal law"). *Cf. In re Fulwiler*, 624 F.2d 908 (9th Cir. 1980) (nondischargeability proceeding in bankruptcy is not one in tort or contract to which state law providing for attorney's fees should apply).

After a debtor files a Chapter 11 petition, he is protected by the automatic stay provision of 11 U.S.C. § 362(a) until an adequate plan takes hold. *See* Revisor's Note to 11 U.S.C. § 362. *See also, In re BBT*, 11 B.R. 224, 232 (Bankr. D. Nev. 1981). To obtain relief from an automatic stay, a creditor may bring a request pursuant to 11 U.S.C. § 362(d). Section 362(d) provides:

> On request of a party in interest and after notice and a hearing, the court shall grant relief from the stay provided under subsection (a) of this section, such as by terminating, annulling, modifying, or conditioning such stay—
>
> > (1) for cause, including the lack of adequate protection of an interest in property of such party in interest; or

> (2) with respect to a stay of an act against property, if—
>
> (A) the debtor does not have an equity in such property; and
>
> (B) such property is not necessary to an effective reorganization.

11 U.S.C. 362(d).

Stay litigation is limited to issues of the lack of adequate protection, the debtor's equity in the property, and the necessity of the property to an effective reorganization. Hearings on relief from the automatic stay are thus handled in a summary fashion. *In re Cedar Bayou, Ltd.*, 456 F. Supp. 278, 284 (W.D. Pa. 1978). The validity of the claim or contract underlying the claim is not litigated during the hearing. The action seeking relief from the stay is not the assertion of a claim which would give rise to the right or obligation to assert a counterclaim. *In re Essex Properties, Ltd.*, 430 F. Supp. 1112 (N.D. Cal. 1977). *See* S. Rep. No. 989, 95th Cong., 2d Sess. 55, *reprinted in* 1978 U.S. Code Cong. & Ad. News, 5787, 5841. Thus, the state law governing contractual relationships is not considered in stay litigation.[2]

State law, therefore, is not ordinarily applied by the bankruptcy court to an action brought pursuant to 11 U.S.C. § 362(d). The Righettis' action, brought pursuant to 11 U.S.C. § 362(d), was predicated solely upon a federal statute and California state law was not applied to any of the substantive issues involved. Thus, the bankruptcy court should not have applied the state substantive law awarding attorney's fees in this case. It is true that the bankruptcy court has authority to apply either state substantive law or federal substantive law, but the

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[2] Furthermore, when a party requests relief from the automatic stay he is not necessarily seeking to foreclose under a contract. Such an action could be brought by one seeking to proceed upon an alleged personal injury claim against the debtor or a variety of other claims not based on contract.

choice depends on the nature of the action involved. *See, e.g., In re Sparkman*, 703 F.2d 1097, 1100 (9th Cir. 1983) (because California state law governed the substantive issues involved in Sparkman's counterclaim filed in proof of claim litigation, it was appropriate to award attorney's fees under state statute); *In re Sonoma V*, 23 B.R. 789, 796 (Bankr. 9th Cir. 1982) (when a federal bankruptcy court exercises jurisdiction over a dispute involving state law (breach of contract action), state law with respect to attorney's fees applies). When, as here, federal and not state law governed the substantive issues involved in the Righettis' motion, the bankruptcy court should not have awarded attorney's fees pursuant to a state statute. *Cf. Alyeska Pipeline Service Co. v. Wilderness Society*, 421 U.S. 240, 259 n.31 (1975) (award of attorney's fees in federal litigation reversed as contrary to the "American Rule" followed by federal courts under which attorney's fees are not recoverable by prevailing litigant in the absence of contrary federal statutory authorization—however, in diversity cases where state law governs, state provisions for such fees may be applied).

The Johnsons contend that this circuit applied section 1717 in a bankruptcy case, *In re Eastview Estates II*, 713 F.2d 443 (9th Cir. 1983), brought under a federal statute—i.e., 11 U.S.C. § 502(b)(1). Section 502(b)(1), however, provides that a court "shall allow" a claim, proof of which has been filed, "except to the extent that . . . such claim is unenforceable against the debtor . . . under any . . . applicable law. . . ." 11 U.S.C. § 502(b)(1). Thus, in proof of claim litigation under 11 U.S.C. § 502(b)(1), the validity of the claim is determined under state law. Such is not the case in stay litigation under section 362(d). Indeed, in *In re Eastview Estates II*, the allowability of the brokers' claims against the estate under section 502(b)(1) turned on whether the brokers had a commission agreement enforceable under California law. 713 F.2d at 447. Because California law

was applied to determine the substantive issues in that case, the court then applied California Civil Code section 1717 in determining the award of attorney's fees. *Id.* at 451. Thus, the principal case relied upon by the Johnsons is not dispositive in this case. The question is whether state law governed the substantive issues of the case. In an action "on the contract," state law necessarily would, but this was not an action "on the contract."

Therefore, because federal law governs the disposition of this relief from stay action, it should also govern disposition of the attorney's fee issue in this case. No federal statute provides for an allowance of attorney's fees to debtors in circumstances such as in this case.[3] Furthermore, there is no evidence or allegation of bad faith or harassment on the part of the Righettis. *See In re* Fulwiler, 624 F.2d 908, 910 (9th Cir. 1980). Thus, because in the absence of a federal statute to the contrary, federal courts follow the "American Rule," under which attorney fees are not recoverable by the prevailing litigant, *Alyeska Pipeline Service Co. v. Wilderness Society*, 421 U.S. 240, 247, 269-71 (1975), the Johnsons are not entitled to recover the attorney fees incurred in opposing the request for relief from the automatic stay.

The district court's decision denying the Johnsons their attorney fees was therefore correct. A request for relief from the automatic stay pursuant to 11 U.S.C. § 362(d) is not an "action on a contract" to which state substantive law would be applied but an action on a federal statute to be decided according to federal law.

The order of the district court is AFFIRMED.

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[3] The Johnsons argue that because the Righettis may have been able to recover attorney's fees under 11 U.S.C. § 506(b), the debtors should be allowed to recover their attorney's fees. This argument is inapposite. Section 506(b) concerns only the award of attorney's fees to oversecured creditors with a contractual right to reimbursement and is not applicable to the Johnsons. *See In re Carey*, 8 B.R. 1000, 1002-04 (Bankr. S.D. Cal. 1981) (court did not construe section 506(b) to incorporate state law on the availability of attorney's fees.)

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

WILLIAM L. WHITTAKER, CLERK

Nos. 84-1811, 84-1817

DC No. C-83-5720 AJZ

IN RE: DON C. JOHNSON and ELIZABETH JOHNSON,
Debtors,

DON C. JOHNSON and ELIZABETH A. JOHNSON,
Appellants,

vs.

MILTON RIGHETTI, *et al.*,
Appellees.

[Filed April 23, 1985]

Appeal from the United States District Court
for the Northern District of California

JUDGMENT

THIS CAUSE came on to be heard on the Transcript of the Record from the United States District Court for the Northern District of California and was duly submitted.

ON CONSIDERATION WHEREOF, It is now here ordered and adjudged by this Court, that the judgment of the said District Court in this Cause be, and hereby is affirmed.

Filed and entered March 28, 1985

UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF CALIFORNIA

No. C-83-5720 AJZ

No. C-84-0248 AJZ

IN RE: DON C. JOHNSON and ELIZABETH JOHNSON,
Debtors,

MILTON RIGHETTI, *et al.*,
Appellants,

vs.

DON C. JOHNSON and ELIZABETH C. JOHNSON,
Appellees.

[Filed Feb. 16, 1984]

ORDER AFFIRMING IN PART
AND REVERSING IN PART
THE DECISION OF THE
BANKRUPTCY COURT

Creditors have brought this appeal from the bankruptcy court's denial of their request for relief from the automatic stay provision of the Bankruptcy Code (11 U.S.C. § 362(d) and from the award of $1100.00 in attorney's fees incurred by the debtor in opposing the request. This court affirms the decision denying relief from the stay and reverses the award of attorney's fees.

It is within the discretion of the bankruptcy court to grant relief from the automatic stay provision of section

362. *In re Holtkamp*, 669 F.2d 505 (7th Cir. 1982). There was no abuse of discretion in this case. Section 362(d) provides that creditors may obtain relief from the automatic stay "for cause, including the lack of adequate protection of an interest in property . . . [or if] the debtor does not have an equity in such property and such property is not necessary to an effective reorganization." Debtors clearly had a substantial amount of equity in the property over which creditors held a deed of trust. Although creditors cite cases in which relief was granted "for cause" where the debtors had not made current payments for more than two years (*In re Galbraith*, 19 B.R. 563, 565 (1982)), or for ten months (*In re Hinkle*, 14 B.R. 202, 204 (1981)), these cases do not support the argument that the bankruptcy court *abused its discretion* in denying relief in this case where debtors recommended making current payments after nine months, creditors are adequately secured, and it appears that debtors' cash flow problems are resolving.

The bankruptcy court awarded debtors their attorney's fees incurred in opposing the motion for relief from the automatic stay. It based the award upon California Civil Code section 1717 which provides: "*In any action on a contract*, where the contract specifically provides that attorney's fees and costs, which are incurred to enforce the provisions of that contract, shall be awarded either to one of the parties or to the prevailing party, then the party who is determined to be the prevailing party, whether he or she is the party specified in the contract or not, shall be entitled to reasonable attorney's . . . ." (emphasis added) Since the promissory note held by creditors and the deed of trust securing it contained attorney's fees provisions in favor of creditors, and since creditors were seeking relief from the automatic stay in order to foreclose under the deed of trust,

the bankruptcy judge reasoned that debtors were entitled to recover their attorney's fees under section 1717 since the request for relief from the stay was denied. This reasoning ignores the opening phrase of the statute. On its face, the statute applies to actions "on a contract." Creditors' motion for relief from the automatic stay was based on a statute, not on a contract. Thus, section 1717 is not applicable.

Accordingly,

IT IS ORDERED that the decision of the bankruptcy judge denying the motion for relief from the automatic stay is affirmed.

IT IS FURTHER ORDERED that the award of attorneys' fees is reversed.

Dated: February 16, 1984

/s/ Alfonso J. Zirpoli
United States District Judge

UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF CALIFORNIA

No. C-83-5720 AJZ

No. C-84-0248 AJZ

IN RE: DON C. JOHNSON and ELIZABETH A. JOHNSON,
Debtors,

MILTON RIGHETTI, *et al.*,
Appellants,

vs.

DON C. JOHNSON and ELIZABETH C. JOHNSON,
Appellees.

[Filed Mar. 27, 1984]

ORDER DENYING MOTION
FOR REHEARING

Debtors filed a "Motion to Amend" the order entered on February 16, 1984, in which the court reversed the decision of the bankruptcy court awarding debtors attorney's fees incurred in defending against creditors' motion for relief from a stay. The court will treat this as a motion for rehearing brought under Bankruptcy Rule 8015.

Debtors base their contention that the court's order reversing the award of attorney's fees was incorrect on the fact that *creditors* would have been entitled to an award of attorney's fees if they had prevailed on the

request for relief from the automatic stay. From this premise, they argue California Civil Code § 1717 requires that *debtors* be entitled to recover their attorney's fees when the bankruptcy court denies a creditor's application for relief from the automatic stay. While debtors' premise is correct, their conclusion does not follow. As stated in the order reversing the award of attorney's fees, section 1717 applies to "actions on a contract." A request for relief from the automatic stay, brought under 11 U.S.C. § 362(d), is not an action on a contract, even though it is certainly a prerequisite to any such action on a contract. The fact that creditors would have been able to recover their attorney's fees under the contractual provision requiring debtors to pay all costs of enforcing the promissory note is simply irrelevant to the question of whether a motion for relief from a stay is an "action on a contract." Since the California statute applies only to actions on a contract, it does not provide that debtors may recover their attorney's fees incurred in successfully defending against a creditor's request for relief from the stay.

Debtors also advance a policy argument which the court finds unpersuasive. They argue that failure to award attorney's fees to the debtor in circumstances such as this "would shift the cost of defending non-meritorious actions for relief from the stay from the unsuccessful creditor to the [other] unsecured creditors of the estate." While this statement may well be true, there is no indication that Congress has sought to prevent the shifting of such costs under the Bankruptcy Code. If Congress wished to prevent such cost shifting due to policy considerations, it would have done so in the Bankruptcy Act. It would not have left the implementation of such a policy to the fortuity that the state in which the debtor lives has a statute such as Civil Code § 1717, or to the fortuity that there is even a provision for the award of attorney's fees in the contract between the creditor and the debtor.

Thus, debtors' policy argument does not justify an award of attorney's fees to debtors in this case.

Accordingly,

IT IS ORDERED that debtors' motion for rehearing is denied.

Dated: March 27, 1984

/s/ Alfonso J. Zirpoli
United States District Judge

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF CALIFORNIA

Case No. 1-82-01460

Adversary No. 1-83-0413

IN RE: DON C. JOHNSON and ELIZABETH A. JOHNSON,
Debtor,

MILTON RIGHETTI, *et al.*,
Plaintiff,

vs.

DON C. JOHNSON and ELIZABETH A. JOHNSON,
Defendants.

[Filed Aug. 30, 1983]

FINDINGS OF FACT, CONCLUSIONS OF LAW AND ORDER FOR JUDGMENT

This action was tried before the Honorable Conley S. Brown, United States Bankruptcy Court, sitting without a jury. Misuraca, Beyers & Costin and Nancy L. Case appeared on behalf of defendant debtors and William C. Johnson appeared on behalf of plaintiffs. This trial was argued and submitted; and the court announced its oral findings of fact, conclusions of law in favor of defendants. The court therefore makes its findings of fact, conclusions of law and order for judgment as follows:

FINDINGS OF FACT

1. The value of the real property which is the security for plaintiffs' promissory note is many times greater than the total amount of debtors' obligation to plaintiffs.

2. The debtors' have an equity in the property of approximately $136,000.00 to $298,000.00.

3. Debtors' are entitled to attorneys' fees as the prevailing parties in this action pursuant to the terms of the promissory note and deed of trust.

CONCLUSIONS OF LAW

1. Plaintiffs are more than adequately secured and have adequate assurances of debtors' ability to repay the the obligation.

ORDER FOR JUDGMENT

Let judgment be entered accordingly denying plaintiffs' request for relief from the automatic stay and awarding defendants their attorneys' fees and costs of suit incurred in this proceeding, pursuant to cost bill.

Dated: August 30, 1983.

/s/ Conley S. Brown
THE HONORABLE CONLEY S. BROWN
United States Bankruptcy Court Judge

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF CALIFORNIA

Case No. 1-83-01460
(Chapter M)

Adversary No. 1-83-0413

IN RE: DON C. JOHNSON and ELIZABETH A. JOHNSON,
Debtor,

MILTON RIGHETTI, *et al.*,
Plaintiff,

vs.

DON C. JOHNSON and ELIZABETH A. JOHNSON,
Defendants.

[Filed Aug. 30, 1983]

[Judgment Entered on Sep. 2, 1983]

ORDER DENYING RELIEF FROM AUTOMATIC STAY

This action was tried before the Honorable Conley S. Brown, United States Bankruptcy Court, sitting without a jury Misuraca, Beyers & Costin and Nancy L. Case appeared on behalf of defendant debtors and William C. Johnson appeared on behalf of plaintiffs. This trial was argued and submitted and the court announced its oral findings of fact, conclusions of law in favor of defendants. Based on the written findings of fact conclusions of

law and order for judgment filed herewith, the court renders the following judgment:

1. Relief from the automatic stay is hereby denied;

2. Defendants are awarded attorneys' fees and costs and are directed to submit a cost bill within ten days from the date of entry of this order.

Dated: August 30, 1983

/s/ Conley S. Brown
THE HONORABLE CONLEY S. BROWN
United States Bankruptcy Court Judge